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UNITED DRUG, INC.

ANNUAL REPORT

DECEMBER 31, 1939

MRB
CORP. FILE

March 1, 1940

To the Stockholders of United Drug, Inc.:

The annual report of your company, herewith submitted, presents a consolidated balance sheet, consolidated statement of profit and loss and earned surplus for the year ended December 31, 1939.

The assets and liabilities and operating profits of our English and South African companies are not included in the accompanying statements. Our investment in these companies is shown separately on the balance sheet.

Earnings for 1939 were $1,063,249.19 or 76¢ per share on the capital stock of the company after providing for depreciation, federal income taxes, bond interest, and loss on guaranteed leases. These figures include $120,323.67, expressed in U. S. dollars, of earnings of the Canadian companies.

Earned Surplus as of December 31, 1939 amounted to $7,585,151.54 and includes a credit of $109,691.55 for discount on United Drug Company bonds purchased during the year and reflects a charge of $159,189.48 covering the decrease in dollar value of net current assets of Canadian companies due to exchange rates.

The profits of the company were charged with taxes amounting to $1,671,314.40 or $1.19 per share. In addition, your company paid various sales taxes amounting to $824,549.17, a portion of which was recovered in selling prices.

It will be noted that working capital amounts to $25,654,514.71. Cash and marketable securities at the end of the year amounted to $9,402,466.44.

With the approval of our Board of Directors, we further reduced our goodwill account by $1,200,000, deducting this from capital surplus. In 1937 our goodwill account was reduced by $2,901,169.38.

On March 29, 1939 the Directors of the Company approved the adoption of a new by-law which provided for the creation of a committee on audits of the Board of Directors. This committee is composed of directors who are not officers of the company.

Respectfully submitted,

Louis K Liggett

President.

PRICE, WATERHOUSE & CO.

75 FEDERAL STREET
BOSTON

February 26, 1940

To the Board of Directors
of United Drug, Inc.:

We have examined the consolidated balance sheet of United Drug, Inc. and its subsidiary companies as at December 31, 1939 and the consolidated statement of profit and loss and earned surplus for the year then ended, have reviewed the system of internal control and the accounting procedures of the companies and, without making a detailed audit of the transactions, have examined or tested accounting records of the companies and other supporting evidence, by methods, at times, and to the extent we deemed appropriate. Our examination included the verification of cash and securities by certificates obtained from the depositaries or by inspection, observations and test counts of the inventories during the year and test confirmations of a substantial portion of the receivables by correspondence with the debtors.

In our opinion, the accompanying consolidated balance sheet and related consolidated statement of profit and loss and earned surplus present fairly the position of United Drug, Inc. and its subsidiary companies at December 31, 1939 and the results of their operations for the year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

PRICE, WATERHOUSE & CO.

UNITED DRUG, INC.

AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENT OF PROFIT AND LOSS AND EARNED SURPLUS FOR THE YEAR ENDING DECEMBER 31, 1939

Sales, less returns, allowances and discounts		$89,356,381.12
Cost of sales, selling, general and administrative expenses (*including depreciation of* $1,204,421.10)		85,775,983.42
Profit from operations		$ 3,580,397.70
Other income:		
Income from investments	$ 17,085.62	
Interest on notes receivable, etc.	41,465.60	
Refunds of federal income taxes for prior years	26,859.85	
Miscellaneous (*net*)	26,931.89	112,342.96
		$ 3,692,740.66
Other charges:		
Interest on funded debt	$1,731,936.46	
Loss from operation of guaranteed leases	464,367.34	
Provision for miscellaneous investments	31,299.15	
Provision for contingencies	83,388.52	
Federal and foreign income taxes	318,500.00	2,629,491.47
Net profit for the year before deducting unrealized Canadian exchange losses charged to surplus below (*See footnote*)		$ 1,063,249.19
Balance, December 31, 1938, of consolidated earned surplus of United Drug, Inc. and subsidiary companies	$6,715,185.41	
Less — Portion included therein represented by undistributed surplus earnings of the English and South African subsidiaries, eliminated from consolidation at December 31, 1939	143,785.13	
Balance, December 31, 1938, of consolidated earned surplus of United Drug, Inc. and domestic and Canadian subsidiaries		6,571,400.28
Discount on purchase of bonds of United Drug Company during the year		109,691.55
		$ 7,744,341.02
Deduct:		
Unrealized exchange losses at December 31, 1939 resulting from the conversion of net assets of Canadian subsidiaries into U. S. dollars		159,189.48
Balance, December 31, 1939, of consolidated earned surplus of United Drug, Inc. and domestic and Canadian subsidiaries, carried to balance sheet		$ 7,585,151.54

Note: The net profit for the year includes $120,323.67, expressed in U. S. dollars, of earnings of Canadian subsidiaries which have not been realized through distribution of dividends to the domestic parent company.

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CONSOLIDATED BALANCE S

ASSETS

CURRENT ASSETS:			
Cash in banks and on hand		$ 8,934,884.80	
Marketable securities and call loan (*value based on December 31, 1939 market quotations, approximately $563,000*)		467,581.64	
Accounts and notes receivable:			
Customers' accounts and notes	$4,808,606.49		
Miscellaneous	359,369.61		
	$5,167,976.10		
Less — Reserves for doubtful balances, discounts, etc.	352,203.34	4,815,772.76	
Inventories of merchandise, partly finished stocks, materials and supplies — at cost or market whichever lower		18,342,157.59	$32,560,396.79
INVESTMENTS AND ADVANCES, ETC.:			
Customers' non-current notes receivable and advances, less reserves		$ 250,488.77	
Miscellaneous advances, claims and deposits, less reserves (*including $80,524.96 due from employees*)		780,856.61	
Investments in and advances to English and South African subsidiaries, wholly owned (*book value of underlying net assets expressed in U. S. dollars, $375,997 — per accompanying notes to financial statements*)		325,036.40	
Miscellaneous investments, at or below cost, less reserves		145,683.31	1,502,065.09
PROPERTY ACCOUNTS — at cost, written down amounts, or appraisal valuations (*including store fixtures and improvements of retail companies at appraisal valuations determined in 1933, as approved by the directors, plus subsequent additions at cost*):			
Land, buildings, and building fixtures		$ 9,370,799.08	
Machinery and equipment, etc.		8,658,711.01	
Store fixtures and improvements		10,247,928.85	
		$28,277,438.94	
Less — Reserves for depreciation		13,253,577.34	15,023,861.60
PREPAID INSURANCE, TAXES, RENT, ETC., AND ADVERTISING SUPPLIES			720,131.53
GOODWILL, TRADE-MARKS, ETC. (*after deducting from the balance of $7,500,000 at December 31, 1938, $217,586.18 of the English subsidiary, eliminated from consolidation, and $982,413.82 of domestic subsidiaries charged to capital surplus, per accompanying statement*)			6,300,000.00
			$56,106,455.01

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HEET—DECEMBER 31, 1939

LIABILITIES

CURRENT LIABILITIES:		
Accounts payable, accrued expenses, etc.	$ 6,085,251.58	
Accrued interest on funded debt	495,573.31	
Reserve for federal and foreign income taxes	325,057.19	$ 6,905,882.08
FUNDED DEBT:		
Twenty-five year 5% debenture bonds of United Drug Company, due March 15, 1953:		
Authorized and issued, $40,000,000 less $4,500,000 retired	$35,500,000.00	
Less — In treasury, held for retirement (*including $750,000 principal amount available to meet the annual sinking fund payment due March 15, 1940*)	1,524,000.00	33,976,000.00
RESERVES:		
Maintenance of store fixtures and improvements	$ 192,611.97	
Contingencies — per accompanying statement	283,988.95	
Miscellaneous	101,140.41	577,741.33
CAPITAL STOCK AND SURPLUS:		
Capital stock:		
Authorized and issued — 1,400,560 shares, par value $5 each	$ 7,002,800.00	
Capital surplus — per accompanying statement	588,319.29	
Earned surplus since September 1, 1933 (*representing principally surplus earnings of subsidiary companies since that date which have not been distributed to the parent company*) — per accompanying statement	7,585,151.54	
	$15,176,270.83	
Less — Cost of 48,973 shares of capital stock of United Drug, Inc. acquired and held by subsidiary company for corporate purposes	529,439.23	14,646,831.60
CONTINGENT LIABILITY:		
United Drug, Inc. and certain other companies organized in 1933 pursuant to a Plan of Reorganization of Drug Incorporated (*since dissolved*) have agreed to assume liability for obligations which may be lawfully established against Drug Incorporated.		
		$56,106,455.01

UNITED DRUG, INC.
AND SUBSIDIARY COMPANIES

NOTES TO FINANCIAL STATEMENTS — DECEMBER 31, 1939

The accompanying consolidated balance sheet and statement of profit and loss and earned surplus include the accounts of the parent company's domestic and Canadian subsidiaries. The English and South African subsidiaries, included in the consolidation at December 31, 1938, have been excluded from consolidation in the 1939 accounts. The investment in these companies is shown in one amount in the consolidated balance sheet.

The following is a condensed statement of foreign assets and liabilities at December 31, 1939, expressed in U. S. dollars, of (1) the Canadian subsidiaries combined and (2) the English and South African subsidiaries combined:

	Canadian subsidiaries combined (*assets and liabilities included in the consolidated balance sheet*)	English and South African subsidiaries combined (*carried as an investment in the consolidated balance sheet*)
Current assets (*including $255,630 of cash and marketable securities of Canadian subsidiaries*)	$1,549,592	$469,875
Current liabilities	310,135	138,397
Net current assets	$1,239,457	$331,478
Fixed properties and other assets	1,145,745	44,519
Total (excess of assets over liabilities)	$2,385,202	$375,997

In addition to the above, the consolidated cash and marketable securities include $48,935 of Canadian and English bank balances and $69,983 of English securities held by domestic subsidiaries.

The current assets, current liabilities, investments, etc., and prepaid expenses in foreign countries have been converted into U. S. dollars at quoted current rates of exchange as at December 31, 1939. Fixed properties have been converted at the average of approximate rates current at the various times these properties were acquired. Earnings of foreign subsidiaries have been converted at average rates of exchange for the year.

Earnings of the English and South African subsidiaries for the year, amounting to approximately $24,000 in U. S. dollars, have not been reflected in the statement of profit and loss and no provision has been made for the decline in dollar net worth of these companies resulting from the conversion of their assets and liabilities at year-end exchange rates, inasmuch as their dollar net worth at December 31, 1939, after conversion, was in excess of the stated amount of the parent company's investment.

UNITED DRUG, INC.
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENT OF CAPITAL SURPLUS FOR THE YEAR ENDING DECEMBER 31, 1939

Balance, December 31, 1938, of consolidated capital surplus of United Drug, Inc. and subsidiary companies	$ 980,215.21
Less — Capital surplus of the English and South African subsidiaries eliminated from consolidation	170,840.23
Balance, December 31, 1938, of consolidated capital surplus of United Drug, Inc. and domestic and Canadian subsidiaries	$ 809,374.98
Add:	
Amounts transferred as at December 31, 1939 from reserves for contingencies per accompanying statement	761,358.13
	$1,570,733.11
Deduct:	
Write-down of the book value of goodwill, trade-marks, etc. as at December 31, 1939, as approved by the directors	982,413.82
Balance, December 31, 1939, of consolidated capital surplus of United Drug, Inc. and domestic and Canadian subsidiaries, carried to balance sheet	$ 588,319.29

CONSOLIDATED STATEMENT OF RESERVES FOR CONTINGENCIES FOR THE YEAR ENDING DECEMBER 31, 1939

Balance, December 31, 1938		$1,011,958.56
Deduct — Charges for the year:		
Payment to cancel lease, made by a subsidiary company and applicable to the period prior to its acquisition	$ 50,000.00	
Portion of the reserve transferred to capital surplus — per accompanying statement	761,358.13	811,358.13
Balance, of which $100,000 represents the remainder of the reserve created on the acquisition of certain subsidiaries in 1933 and $100,600.43 represents amounts provided by charges to profit and loss since their acquisition and since the inception of United Drug, Inc.		$ 200,600.43
Add:		
Amount provided by charges to profit and loss in the current year		83,388.52
Balance, December 31, 1939, per balance sheet		$ 283,988.95

OFFICERS

Louis K. Liggett	*President*
Joseph A. Galvin	*Vice-President & Treasurer*
W. Newlin Mitchell	*Assistant Treasurer*
William F. Davis, Jr.	*Secretary*

DIRECTORS

Charles Francis Adams	*Chairman*, Board of Directors, State Street Trust Company, Boston
George M. Gales	*Chairman*, Executive Committee, Liggett Drug Co., Inc., New York
George C. Haigh	*Vice-President*, Bank of the Manhattan Company, New York
Louis K. Liggett	*President*, Boston
Thomas H. McInnerney	*President*, National Dairy Products Corporation, New York
Warren Motley	Gaston, Snow, Hunt, Rice and Boyd, Boston
Charles S. Munson	*President*, U. S. Industrial Alcohol Company, New York *President*, Air Reduction Co., Inc., New York
James L. Richards	*Chairman Board of Directors*, Boston Consolidated Gas Company, Boston
Fred S. Rogers	Rogers Drug Stores, Inc., Middletown, New York
Eugene W. Stetson	*Vice-President*, Guaranty Trust Company of New York, New York

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Transfer Agents

Guaranty Trust Company of New York, New York

State Street Trust Company, Boston

Registrars

The Chase National Bank of the City of New York, New York

The National Shawmut Bank of Boston, Boston

Counsel

Gaston, Snow, Hunt, Rice and Boyd, Boston

Root, Clark, Buckner and Ballantine, New York